No. 91-1671

In The
Supreme Court of the United States
October Term, 1992

WILLIAM J. MERTENS, ALEX W. BANDROWSKI, JAMES A. CLARKE, and RUSSELL FRANZ,

Petitioners,

v.

HEWITT ASSOCIATES, an Illinois Partnership,

Respondent.

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

BRIEF FOR THE PETITIONERS

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QUESTION PRESENTED

Whether a nonfiduciary who knowingly participates in a breach of fiduciary duty under the Employee Retirement Income Security Act of 1974 is liable for losses that an employee benefit plan sustains as a result of the breach.

PARTIES TO THE PROCEEDING

In addition to the parties named in the caption of this petition, the petitioners sued two other parties: the Kaiser Steel Retirement Plan ("Plan"), and the Pension Benefit Guaranty Corporation ("PBGC"), which had terminated the Plan pursuant to ERISA's distress termination provisions. Petitioners sued the PBGC in its capacity as the Plan's statutory trustee. The PBGC answered and filed a cross-claim in which it asserted that any recovery by the plaintiffs should be paid to it. The district court granted Hewitt's motion for dismissal of the PBGC's cross-claim as "derivative" of the complaint. *Sua sponte*, the district court also dismissed the Plan and the PBGC "since no distinct allegations were directed against them. . . . " (J.A. 32). The PBGC did not appeal on behalf of the Plan or itself as the statutory trustee.

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OPINIONS BELOW

The opinion of the Court of Appeals for the Ninth Circuit is reported at 948 F.2d 607, and is reprinted in the Joint Appendix at pp. 35-49.

The memorandum decision of the United States District Court for the Northern District of California (Patel, D.J.) has not been reported. It is reprinted in the Joint Appendix at pp. 19-33.

JURISDICTION

On January 15, 1992, the court of appeals denied a timely petition for rehearing (J.A. 50), after first granting the Secretary of Labor's Motion for Leave to File her Brief Amicus Curiae in support of rehearing *en banc*. (J.A. 51). On April 14, 1992, petitioners filed a petition for a writ of certiorari which was granted by this Court on October 5, 1992. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

ERISA § 409(a), 29 U.S.C. § 1109(a), provides:

> Any person who is a fiduciary with respect to a plan who breaches any of the responsibilities, obligations, or duties imposed upon fiduciaries by this title shall be personally liable to make good to such plan any losses to the plan resulting from each such breach, and to restore to such plan any profits of such fiduciary which have been made through use of assets of the plan by the fiduciary, and shall be subject to such other equitable or remedial relief as the court may deem appropriate, including removal of such fiduciary. A fiduciary may also be removed for a violation of section 411 of this Act.

ERISA § 502(a), 29 U.S.C. § 1132(a), provides in relevant part:

> A civil action may be brought –
>
> (1) * * *

> (2) by the Secretary, or by a participant, beneficiary or fiduciary for appropriate relief under section 409;
>
> (3) by a participant, beneficiary, or fiduciary (A) to enjoin any act or practice which violated any provision of this title or the terms of the plan, or (B) to obtain other appropriate equitable relief (i) to redress such violations or (ii) to enforce any provisions of this title or the terms of the plan;
>
> (4) * * *
>
> (5) * * * by the Secretary (A) to enjoin any act or practice which violates any provision of this title, or (B) to obtain other appropriate relief (i) to redress such violation or (ii) to enforce any provision of this title;
>
> (6) * * *

ERISA § 502(*l*), 29 U.S.C. § 1132(*l*) provides:

> (1) In the case of (A) any breach of fiduciary responsibility under (or other violation of) part 4 by a fiduciary, or (B) any knowing participation in such a breach or violation by any other person, the Secretary shall assess a civil penalty against such fiduciary or other person in an amount equal to 20 percent of the applicable recovery amount..
>
> (2) For purposes of paragraph (1), the term "applicable recovery amount" means any amount which is recovered from a fiduciary or other person with respect to a breach or violation described in paragraph (1) – (A) pursuant to any settlement agreement with the Secretary, or (B) ordered by a court to be paid by such

fiduciary or other person to a plan or its participants and beneficiaries in a judicial proceeding instituted by the Secretary under subsection (a)(2) or (a)(5).

(3) The Secretary may, in the Secretary's sole discretion, waive or reduce the penalty under paragraph (1) if the Secretary determines in writing that (A) the fiduciary or other person acted reasonably and in good faith, or (B) it is reasonable to expect that the fiduciary or other person will not be able to restore all losses to the plan without severe financial hardship unless such waiver or reduction is granted.

(4) The penalty imposed on a fiduciary or other person under this subsection with respect to any transaction shall be reduced by the amount of any penalty or tax imposed on such fiduciary or other person with respect to such transaction under subsection (i) of this section and section 4975 of the Internal Revenue Code of 1986.

STATEMENT OF THE CASE

The court of appeals in this case held that ERISA does not afford pension plan participants a cause of action against the plan's actuary for knowingly participating in breaches of fiduciary duty committed by the plan's fiduciaries which resulted in the distress termination of the severely underfunded plan. The court's decision, consistent with its earlier opinion in *Nieto v. Ecker*, 845 F.2d 868 (9th Cir. 1988), conflicts directly with the reported decisions of the Second, Sixth, Seventh, and District of Columbia Circuit Courts of Appeals. All of

these courts have recognized the liability under ERISA of non-fiduciaries who knowingly participate in a fiduciary breach. Only the Eleventh Circuit Court of Appeals agrees with the Ninth Circuit in refusing to recognize non-fiduciary liability under ERISA for aiders and abetters of ERISA fiduciary breaches.

Upon taking over the Kaiser Steel Pension Plan pursuant to ERISA's distress termination provision, 29 U.S.C. § 1341, the PBGC stated through its Executive Director that "[t]he company's funding of the plan was grossly inadequate to pay the benefits promised . . . . " (*BNA Pension Reporter*, p. A-5, March 11, 1987). As a result of the Plan's "gross" underfunding, the petitioners, all long-term Kaiser Steel Company ("Kaiser") management employees, suffered substantial reductions in their monthly pension benefits.[1]

The court of appeals opinion sets forth plaintiffs' allegations against defendant, Hewitt Associates ("Hewitt"), the actuary for Kaiser, which it accepted as true in reviewing the district court's dismissal of the action against Hewitt pursuant to F.R.Civ.P. 12(b)(6):

> . . . Kaiser hired Hewitt to perform actuarial work for its ERISA plan. Early in 1980, Kaiser restructured its business operations and virtually eliminated its steel-making operations. As a result, the number of employees retiring

[1] Petitioner Mertens suffered a reduction in his monthly pension from $2,016.00 to $521.00, petitioner Bandrowski from $1,907.00 to $670.00, petitioner Clarke from $2,567.00 to $1,103.00, and petitioner Franz from $1,426.00 to $478.00. (J.A. 6-7).

from the company who were entitled to early retirement benefits under the plan increased significantly, as did the plan's funding costs.

The actuarial assumptions Hewitt had developed previously for the plan did not reflect the increased costs, and Hewitt did not change its assumptions to reflect the increase. Rather, Hewitt delegated the responsibility for selecting actuarial assumptions to Kaiser.

According to the plaintiffs, Hewitt's conduct was improper. Had Hewitt employed proper actuarial assumptions, Kaiser would have had to make substantially higher contributions to the plan. Hewitt failed to disclose this funding inadequacy in any certificate or other writing which it prepared on behalf of the plan. As a consequence of Hewitt's acts and omissions, Kaiser failed to fund the plan adequately, and the plan's assets became insufficient to satisfy benefit commitments, including the commitment to pay the plaintiffs their fully vested pensions. (J.A. 36-37).

Plaintiffs further alleged: that Hewitt did actuarial work for Kaiser Steel at the same time it performed services for the plan; that Hewitt did not want to jeopardize its lucrative professional relationship with Kaiser; and that Hewitt failed to disclose to plan administrators its relationship with Kaiser or the potential conflict that the relationship created. (J.A. 36-37).

Plaintiffs asserted three separate legal theories under ERISA against Hewitt:

(a) Hewitt breached its fiduciary duties to the Plan;

(b) Hewitt knowingly participated in a breach of fiduciary duty; and,

(c) Hewitt breached its actuarial duties to the Plan. (J.A. 38).

Plaintiffs also alleged that Hewitt committed professional malpractice under California law and invoked the Court's pendent jurisdiction. (J.A. 38).[2]

On March 7, 1990, Hewitt moved to dismiss the Complaint under F.R.Civ.P. 12(b)(6) on the grounds that the Complaint failed to state an ERISA claim for which relief could be granted and that the applicable California statute of limitations barred plaintiffs' pendent state law claim for professional malpractice.

On August 9, 1990, the district court dismissed all of petitioners' claims and entered judgment for respondent. (J.A. 31-32). The district court held that Hewitt could not be held responsible for losses suffered by plaintiffs because: (1) the facts alleged in the complaint did not warrant a finding that Hewitt acted as a fiduciary under ERISA; (2) ERISA provides no remedy against a non-fiduciary who participates in a breach of fiduciary duty; (3) ERISA provides no remedy for Hewitt's alleged breach of professional actuarial duties; and (4) the California statute of limitation barred plaintiffs' state law malpractice claim.

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[2] The plaintiffs did not appeal to the Ninth Circuit their claim, dismissed by the district court, that Hewitt had engaged in a party-in-interest transaction prohibited by ERISA. (J.A. 29-30).

Petitioners filed a timely Notice of Appeal on August 25, 1990. On November 4, 1991, the Ninth Circuit affirmed the dismissal of all of petitioners' ERISA-based claims, but reversed the district court's dismissal of petitioners' pendent state professional malpractice claim. (J.A. 49).[3]

Petitioners sought certiorari only with respect to the court of appeals holding, based on *Nieto v. Ecker*, 845 F.2d 868 (9th Cir. 1988), that non-fiduciaries are not liable under ERISA for knowingly participating in fiduciary breaches.

The court of appeals concluded that Congress' enactment of the Omnibus Budget Reconciliation Act ("OBRA") of 1989, adding a new ERISA enforcement provision, 29 U.S.C. § 1132(*l*), did not confirm Congress's original intent to permit suits against non-fiduciaries who knowingly aid and abet a fiduciary in the commission of a breach of fiduciary duty. (J.A. 41-44).

Noting that section 1132(*l*) applies "to the Secretary only, not to plan participants" (J.A. 43), the Ninth Circuit declined to read the recent Congressional enactment as indicating that sections 502(a)(3) and (5), 29 U.S.C. §§ 1132(a)(3) and (5), had always imposed liability on a non-fiduciary who knowingly aids and abets an ERISA fiduciary in breaching his ERISA duties. (J.A. 43-44). Rather, the court held that the amendment *created*, for the first time, a cause of action by the *Secretary* against non-fiduciaries under §§ 502(a)(3) and (5), but not on behalf of plan participants and beneficiaries. (J.A. 43-44).

[3] Upon remand Hewitt moved to dismiss plaintiffs' California professional malpractice claim on the grounds of preemption. On June 5, 1992, prior to this Court's grant of certiorari, the district court denied Hewitt's motion.

SUMMARY OF THE ARGUMENT

I

Congress' 1989 amendment of ERISA, which requires the Secretary of Labor to assess civil penalties against nonfiduciaries who knowingly participate in a breach of fiduciary duty, confirms Congress' original intent to impose liability on aiders and abettors of fiduciary breaches.

In enacting the Omnibus Budget Reconciliation Act of 1989 ("OBRA"), Congress added a new subsection ("*l*") to ERISA section 502(*l*), 29 U.S.C. 1132(*l*). The amendment requires the Secretary to assess a civil penalty against "knowing participants" in fiduciary breaches "in an amount equal to 20 percent of the *applicable recovery amount*." (emphasis added). The term "applicable recovery amount" is defined in section 1132(*l*)(2) as any amount which is recovered in a proceeding by the Secretary under sections 1132(a)(2) or (5). However, there could be no such "recoveries" from nonfiduciaries unless sections 1132(a)(2) and (a)(5) already encompassed such relief.

Section 1132*(a)(5)* provides for suit by the Secretary to obtain "appropriate equitable relief" to redress violations of the statute or to enforce its provisions. Section 1132*(a)(3)* provides, in the identical language, for such

suits by pension plan participants. If the Secretary has the right to bring an action for monetary relief against nonfiduciaries under section 1132(a)(5), then participants must have the corresponding right to sue nonfiduciaries under section 1132(a)(3). Identical statutory provisions must be given the same effect.

New section 1132(*l*) did not, as the court of appeals believed, *create* a new cause of action against nonfiduciaries in the Secretary alone. Nothing in ERISA's remedial scheme, which gives the Secretary and participants virtually the same enforcement rights, supports such a conclusion. Rather, the amendment simply established a civil penalty scheme, which comes into play only if the Secretary has recovered money from a nonfiduciary under section 1132. Contrary to the Ninth Circuit's holding, section 1132(*l*) confirmed the existence of the underlying cause of action against nonfiduciary aiders and abettors. Adding a mandatory penalty provides further deterrence against both ERISA fiduciaries who breach their duties and nonfiduciaries who knowingly participate in such breaches.

II

ERISA is a "comprehensive statute designed to promote the interests of employees and their beneficiaries in employee benefit plans." *Shaw v. Delta Airlines, Inc.*, 462 U.S. 85, 90 (1983). Section 1132(a)'s provision for "appropriate" equitable relief to "redress" violations of the statute is a clear mandate to the courts to fashion all remedies which are appropriate to enforce the Act. It should be construed to include make-whole relief against

nonfiduciaries who knowingly participate in fiduciary breaches.

The Ninth Circuit read this Court's decision in *Massachusetts Life Ins. Co. v. Russell*, 473 U.S. 134 (1985), too broadly when, in *Nieto v. Ecker*, 845 F.2d 868 (1984), it concluded that the only remedies available to redress breaches of fiduciary duty are those expressly enumerated in the statute. In *Russell*, the Court addressed the question of whether, under ERISA Section 409, 29 U.S.C. 1109, a cause of action for breach of fiduciary duty inures to individuals, or only to a plan. Construing only Section 1109, the Court emphasized the Congressional concern with protecting the assets of the *plan* from fiduciary misconduct. Against this background, the Court was reluctant to infer remedies under section 1109 on behalf of individuals for fiduciary breaches. *Russell* did not consider the scope of the remedies available to individuals or plans under section 1132 to redress violations of the statute.

Since *Russell*, the Court has stated in *Ingersoll-Rand Co. v. McClendon*, 498 U.S. 478 (1990), that the remedial provisions of section 1132 are broad enough to encompass remedies which are not specifically enumerated. Furthermore, in *Firestone Tire and Rubber Co. v. Bruch*, 489 U.S. 101 (1989), the Court held that ERISA's legislative history confirms that ERISA's "fiduciary responsibility provisions" codified principles of trust law. *Firestone* explicitly directs the federal courts to develop a federal common law of "rights and obligations" under ERISA-regulated plans, drawing upon principles of trust law.

Under the law of trusts, a knowing participant in a fiduciary breach is jointly and severally liable for the full amount of the loss sustained. Four other courts of appeals and the great majority of district courts which have considered the issue of nonfiduciary liability under ERISA have held that ERISA incorporates this principle of trust law.

This interpretation of the statute is the most sensible one. ERISA's fiduciary responsibility provisions are at the center of ERISA's remedial scheme. As pointed out by *Russell*, their purpose is to protect plan assets against fiduciary misconduct, and to ensure the rights of those who are promised such benefits. Under traditional trust law, those who knowingly assist a fiduciary in breaching his fiduciary duties are as responsible for the breach as the fiduciary. This Court should not hold that Congress, while enacting powerful proscriptions on fiduciary misconduct, has at the same time chosen to exempt from responsibility those who aid fiduciaries in carrying out violations of ERISA.

III

The Ninth Circuit's interpretation of ERISA provides beneficiaries with less protection than they had before ERISA was enacted. Prior to ERISA, under the law of trusts, courts imposed liability on third persons who knowingly participated in a breach of fiduciary duty.

Incorporation of nonfiduciary liability in the circumstances of this case is consistent with the entire history and purpose of ERISA. It was the need to better protect

pension plan participants that spurred the passage of ERISA and inspired the Congressional mandate for the courts to develop a federal common law in the enforcement of ERISA. Congress envisioned that the courts would develop a body of federal substantive law to enforce the statute and adapt trust law to the particular purposes of employee benefit plans.

Under ERISA, a cause of action against nonfiduciaries who knowingly participate in breaches of fiduciary duty is essential to deter violations of ERISA's fiduciary responsibility provisions, and to ensure that plans can recover losses caused by such violations. Often, fiduciaries cannot carry out violations of ERISA without the cooperation of others. Pension plan participants would be denied full relief if they were unable to recover against nonfiduciary aiders and abettors. Congress did not intend to eliminate this important protection, which was deemed essential to the protection of beneficiaries even before the passage of ERISA.

ARGUMENT

I. CONGRESS'S 1989 AMENDMENT OF ERISA, WHICH REQUIRED THE SECRETARY OF LABOR TO PURSUE CIVIL PENALTIES AGAINST NONFIDUCIARIES WHO KNOWINGLY PARTICIPATE IN FIDUCIARY BREACHES, CONFIRMED ITS ORIGINAL INTENT TO IMPOSE ERISA LIABILITY ON AIDERS AND ABETTERS OF FIDUCIARY BREACHES.

In enacting the Omnibus Budget Reconciliation Act of 1989, Pub. L. No. 101-239, § 201, 103 stat. 123

("OBRA"), Congress added a new subsection ("*l*") to ERISA Section 502, 29 U.S.C. § 1132 (Supp. II 1990). This amendment requires the Secretary of Labor ("the Secretary") to pursue civil penalties against knowing participants in fiduciary breaches, as follows:

> In the case of –
>
> > (A) any breach of fiduciary responsibility under (or other violation of) part 4 of this sub-title by a fiduciary, or
> >
> > (B) **any knowing participation in such a breach or violation by any other person,**
>
> the Secretary shall assess a civil penalty against such fiduciary or other person in an amount equal to 20 percent of **the applicable recovery amount.** (Emphasis added.)

This mandatory civil penalty strengthens the statute by imposing substantial monetary sanctions upon a fiduciary who breaches his duties, and "any other person" who knowingly participates in such breaches. H.R. Conf. Rep. No. 386, 101st Cong., 1st Sess., *reprinted in* 1989 U.S. Code Cong. & Admin. News 3018, 3035-36.

The penalty referred to in Section 1132(*l*) is "an amount equal to 20 percent of the applicable recovery amount." The term "applicable recovery amount" is defined in section 1132(*l*)(2) as:

> any amount which is recovered from a fiduciary or other person with respect to a breach or violation . . . (A) pursuant to any settlement agreement with the Secretary, or (B) ordered by a court to be paid by such fiduciary or other person to a plan or its participants and beneficiaries in a judicial proceeding instituted

> by the Secretary under subsection (a)(2) or (a)(5).

There could be no such "recoveries" from non-fiduciaries, however, unless sections 1132(a)(2) and (5) already encompassed monetary relief from non-fiduciaries. The OBRA amendment thus makes it apparent that the Secretary *always* had the power to institute litigation against non-fiduciaries under subsections (a)(2) and (a)(5).

Section 1132(a)(2) provides that suit may be brought by the Secretary *or* by plan participants for relief under 29 U.S.C. § 1109. Thus, if the Secretary could sue non-fiduciary aiders and abetters under section 1132(a)(2), then plan participants must also have had that right.

Similarly, if the Secretary can bring an action against a non-fiduciary under section 1132(a)(5), then a plan participant must have the corresponding right to sue non-fiduciaries under section 1132(a)(3). The relevant language in sections 1132(a)(3) and (a)(5) is identical; identical statutory language must be given the same effect. See *Estate of Cowart v. Nicklos Drilling Co.*, 112 S.Ct. 2589, 2596 (1992) ("[a] basic canon of statutory construction [is] that identical terms within an Act bear the same meaning."); *Pension Fund-Mid Jersey Trucking Industry-Local 701 v. Omni Funding Group*, 731 F. Supp. 161, 178 n. 11 (D.N.J. 1990) (treating sections 1132(a)(3) and (a)(5) as the same for purposes of implying a cause of action for knowing participation in a breach of fiduciary duty).

In rejecting this analysis, the Ninth Circuit misconstrued the plain language of section 1132(*l*), which does not, as the court incorrectly concluded, *create* a new

cause of action by the Secretary against aiders and abetters. Rather the amendment simply establishes a civil penalty provision, which comes into play only if the Secretary has recovered money from a non-fiduciary either through settlement or through a section 1132(a)(5) judicial proceeding. Contrary to the Ninth Circuit's holding, new section 1132(*l*) confirmed the existence of the underlying cause of action against non-fiduciary aiders and abetters in section 1132(a). *See Red Lion Broadcasting Co. v. FCC*, 395 U.S. 367, 380-381 (1968) ("[s]ubsequent legislation declaring the intent of an earlier statute is entitled to great weight in statutory construction").

Indeed, nothing in ERISA's remedial scheme – which vests virtually co-extensive enforcement rights in both the Secretary and participants – supports the Ninth Circuit's conclusion that Congress intended to afford the Secretary, but not private plan participants and beneficiaries, the exclusive right to recover against non-fiduciaries. As noted, the enforcement language in section 1132(a)(2) applies both to the Secretary and participants; the language in section 1132(a)(3) (relating to participants and beneficiaries) is identical to that in 1132(a)(5) (relating to the Secretary). Nevertheless, the Ninth Circuit declined to read the OBRA amendment to ERISA as indicating that section 1132 always imposed liability on a non-fiduciary who knowingly aids and abets an ERISA fiduciary in breaching his duties. The court concluded that "[i]n drafting the ERISA amendments in 1989, Congress considered but rejected an amendment to overrule our decision in *Nieto*. (Citations omitted.) We decline to do what Congress has refused to do." (J.A. 44).

The court observed that an early version of OBRA, H.R. 3299, would have added a new section 409(c), 29 U.S.C. § 1109(c), explicitly stating that persons who knowingly participate in a breach of fiduciary duty "shall be personally liable to the plan for such breach of fiduciary responsibility in the same manner and to the same extent as if they were a fiduciary committing such breach." H.R. 3299, 101st Cong., 1st Sess., § 3161(e)(6), 135 Cong. Rec. H6006 (daily ed. Sept. 27, 1989). The report on H.R. 3299 states that the purpose of proposed section 409(c) was to resolve "the conflict in the courts of appeal by clarifying Congressional intent to codify in ERISA the common law of trusts as it applies to employee benefit plans." H.R. Rep. No. 247, 101st Cong., 1st Sess., *reprinted in* 1989 U.S. Code Cong. & Admin. News 1906, 1969-70.

Contrary to the Ninth Circuit's conclusion, Congress's omission in the final amendment of language explicitly overruling *Nieto* does not indicate approval of *Nieto*. Such "[c]ongressional inaction lacks 'persuasive significance' because 'several equally tenable inferences' may be drawn from such inaction, 'including the inference that the existing legislation already incorporated the offered change.' " *PBGC v. LTV Corp.*, 496 U.S. 633, 110 S.Ct. 2668, 2678 (1990) (quoting *U.S. v. Wise*, 370 U.S. 405, 411 (1962)). Indeed, at the time Congress enacted OBRA, all of the other circuits which had addressed the issue of non-fiduciary liability had concluded that such liability existed under ERISA. The OBRA amendment that Congress did in fact adopt indicates that Congress approved of these appellate decisions, rather than *Nieto*, as reflecting the correct interpretation of the statutory text as written.

Moreover, in providing for a "waiver" of the civil penalty in section 1132(*l*)(3)(B) Congress could not have made more clear that the phrase "appropriate equitable relief" in §§ 1132(a)(3) and (5) includes the remedy of restoration of "all losses to the plan." Under section 1132(*l*)(3)(B), the Secretary may waive or reduce the civil penalty if imposition of the penalty would interfere with the non-fiduciary's ability "to restore all losses to the plan without severe financial hardship." This waiver criterion would be meaningless if the non-fiduciary were not, in the first instance, liable for "all losses to the plan."

II. THE DECISION BELOW, IN CONFLICT WITH THOSE OF FOUR OTHER CIRCUIT COURTS OF APPEAL, UNDERMINES ERISA'S FIDUCIARY CONDUCT PROVISIONS AND THE UNIFORM NATIONAL APPLICATION OF ERISA'S REMEDIAL PROVISIONS.

ERISA is a "comprehensive statute designed to promote the interests of employees and their beneficiaries in employee benefit plans." *Shaw v. Delta Airlines, Inc.*, 463 U.S. 85, 90 (1983). As this court noted, by enacting ERISA, Congress intended to "preempt the field for Federal regulations, thus eliminating the threat of conflicting or inconsistent State and local regulation of employee benefit plans." *Id.* at 99, citing 120 Cong. Rec. 29,933 (1974) (remarks of Sen. Harrison Williams). The Ninth Circuit's decision to follow *Nieto* conflicts with the decisions of four other courts of appeals and with the decisions of the vast majority of district courts which have addressed the issue of non-fiduciary liability under ERISA.

Non-fiduciary liability under ERISA stems from the broad enforcement authority conferred upon participants,

beneficiaries, and fiduciaries by section 1132(a)(3) and upon the Secretary by section 1132(a)(5) to obtain "appropriate equitable relief" to "redress" violations of the statute or "to enforce" any of its provisions. Congress's broad language requiring federal courts to provide "appropriate" equitable relief is a clear mandate to fashion all remedies which are appropriate to enforce the Act. "The legislative history demonstrates that Congress intended federal courts to develop federal common law in fashioning the additional 'appropriate equitable relief,' " provided for in sections 1132(a)(3) and (5). *Massachusetts Mutual Life Ins. Co. v. Russell*, 473 U.S. 134, 156 (1985) (Brennan, J. concurring). It should be construed to include make-whole relief against non-fiduciaries who knowingly participate in bringing about violations of ERISA.

Nieto was decided without the benefit of *Firestone Tire and Rubber Co. v. Bruch*, 489 U.S. 101 (1989), in which the Court explicitly authorized the development of a federal common law of rights and responsibilities drawing upon principles of trust law. Speaking for the Court, Justice O'Connor emphasized that ERISA's fiduciary responsibility provisions "codified" principles of trust law and that courts were to develop a federal common law of "rights and obligations" drawing upon such principles:

> ERISA abounds with the language and terminology of trust law. . . . ERISA's legislative history confirms that the Act's **fiduciary responsibility provisions**, 29 U.S.C. §§ 1101-1114, "codif[y] and mak[e] applicable to ERISA fiduciaries certain principles developed in the evolution of the law of trusts." H.R. Rep. No. 93-533, p.11 (1973), U.S. Code Cong. &

> Admin. News 1974, pp.4639, 4649. Given this language and history, we have held that courts are to develop "a federal common law of rights and obligations under ERISA regulated plans." *Id.* at 110. (Emphasis added.)

Under the law of trusts, it is a well-established principle that a knowing participant in a fiduciary breach is jointly and severally liable for the full amount of the loss resulting from that breach. See G. Bogert & G. Bogert, The Law of Trusts and Trustees, §§ 868, 901 (rev. 2d ed. 1982); 4 A. Scott, The Law of Trusts, §§ 290-295, 321-326 (3d ed. 1965 & Supp. 1985); Restatement (Second) of Trust, §§ 290-297, 321-326 (1959).

The courts of appeals which have recognized the liability of non-fiduciaries have held that ERISA incorporates this principle from trust law. *Whitfield v. Lindemann*, 853 F.2d 1298, 1303, (5th Cir. 1988), *cert denied sub nom. Klepak v. Dole*, 490 U.S. 1089 (1989) ([A]lthough Klepak was not a statutory fiduciary, he was, as the district court held, jointly liable . . . as a non-fiduciary who knowingly participated in a breach of trust"); *Brock v. Hendershott*, 840 F.2d 339, 342 (6th Cir. 1988) (non-fiduciary liable for assisting fiduciary co-defendant in scheme to cause plans to use assets in ways which benefited defendants); *Lowen v. Tower Asset Management, Inc.*, 829 F.2d 1209, 1220 (2d Cir. 1987) (principals in, and affiliates of, corporation which breached fiduciary duties held liable as knowing participants in breach); *Fink v. National Sav. & Trust Co.*, 772 F.2d 951, 958 (D.C. Cir. 1985) (*dictum*); *Thornton v. Evans*, 692 F.2d 1064, 1078 (7th Cir. 1982) (holding, on a motion to dismiss, that a non-fiduciary, alleged to have conspired with a fiduciary to mislead other fiduciaries

into taking action which harmed plan, can be held liable under ERISA); (citations omitted).[4]

In arriving at a result contrary to that reached by the vast majority of courts addressing the issue of ERISA non-fiduciary liability, the Ninth Circuit in *Nieto* concluded from the liability provisions of section 1109(a) (which provides that "[a]ny person who is a fiduciary" shall be "personally liable" to a plan for any breach of fiduciary duty) that had Congress intended to include non-fiduciaries, it would have done so explicitly. *Nieto*, 854 F.2d at 871-874. The court found, moreover, that interpreting section 1132 to provide causes of action against non-fiduciaries would in effect render section 1109 superfluous, "a result contrary to the fundamental canons of statutory construction." *Id.* at 873.

The Ninth Circuit read *Russell* too broadly when it concluded that the only remedies available to redress fiduciary breaches are those specifically enumerated in the statute. In *Russell* the Court addressed the question of whether, under ERISA section 409, 29 U.S.C. § 1109, a cause of action for breach of fiduciary duty inures to individuals, or only to a plan. Construing section 1109,

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[4] Although decided after the 1989 OBRA amendment, *Useden v. Acker*, 947 F.2d 1563 (11th Cir. 1991), the only appellate decision adopting *Nieto*, does not discuss the effect of that amendment on the issue presented. (Trying to reconcile *Firestone Tire and Rubber Co. v. Bruch*, 489 U.S. 101 (1989), with *Nieto*, the court of appeals held in *Useden* that "a court should only incorporate a given trust law principle if the statute's text negates an inference that the principle was omitted deliberately from the statute".) *Id.* at 1581.

the Court emphasized Congress' concern with protecting the assets of the plan from fiduciary misconduct. Against this background, the Court was reluctant to infer remedies under section 1109 on behalf of individuals for fiduciary breaches. *Russell* did not consider the scope of the remedies available to individuals or plans under section 1132 to redress violations of the statute.

Since *Nieto*, the Supreme Court has analyzed section 1132(a) generally and section 1132(a)(3) in particular. In *Ingersoll-Rand Co. v. McClendon*, 498 U.S. 133, 111 S.Ct. 478 (1990), the Court concluded that the remedial provisions of section 1132 are broad enough to encompass remedies which are *not* specifically enumerated. Although the Court in *Ingersoll* did not discuss in detail what remedies are available as "other appropriate equitable relief" under section 1132(a)(3), the Court stated, "[i]t is clear that the relief requested" – which included a prayer by the plaintiff in that case for compensatory damages – "is well within the power of federal courts to provide." 111 S.Ct. at 486. (dictum) Notably, an award of compensatory damages is not a specifically enumerated remedy under section 1132. In light of *Ingersoll-Rand*, it is apparent that the Ninth Circuit in *Nieto*, and now in this case, incorrectly applied *Russell* to support its holding that the *only* remedies available to redress fiduciary breaches are those specifically enumerated in the statute.

The requirements relating to fiduciary responsibility are the core provisions of the ERISA remedial scheme. Their overriding purpose was to protect pension plan assets against misconduct and to ensure the rights of those who are promised such benefits. As discussed in Part III, *infra*, basic trust law holds those who knowingly

participate with fiduciaries in committing fiduciary breaches as responsible as the fiduciary. Given the entire background and legislative history of ERISA, Congress could not have meant to exempt from liability those who knowingly assist in the commission of fiduciary breaches. No persuasive explanation has been given by the Ninth Circuit or by any other court as to why Congress would enact powerful proscriptions on the conduct of fiduciaries, while, at the same time, completely exempting those who knowingly aid fiduciaries in violating the statute's fiduciary provisions.

A cause of action against non-fiduciaries is essential in order to deter violations of ERISA's fiduciary responsibility provisions and to ensure that plans have the means to attain complete recovery of all losses caused by such violations. See Part III, *infra*. Cf. *Brock v. Gerace*, 635 F. Supp. at 569 (plan's participants would be denied full relief if the Secretary were unable to recover from non-fiduciaries).

The Ninth Circuit also erred in *Nieto* when it focussed almost entirely on section 409 of the Act, 29 U.S.C. § 1109, and section 502(a)(2), 29 U.S.C. § 1132(a)(2) (which, as noted, *supra*, authorizes actions to enforce section 1109) and concluded that the plain language of the statute limited ERISA's coverage to fiduciaries only. *Nieto*, 845 F.2d at 871-874. The court concluded that interpreting section 1132 to provide causes of action against non-fiduciaries would in effect render section 1109 superfluous. *Id.* However, as noted by Judge Wiggins in his opinion concurring in the judgment on other grounds

"[b]y reading section 409(a), 29 U.S.C. § 1109(a), in isolation, [the court] ignores the clear requirement of the Act to provide the broadest possible remedies under ERISA to plan beneficiaries." *Id.* at 875.

That Congress specified a fiduciary's liability in section 1109 does not preclude construing the broad language of sections 1132(a)(3) and (5) to reach a wider class of persons who aid in the commission of a fiduciary breach. As Judge Wiggins also noted, section 1109(a) "is simply one section among many that impose liability on those who violate the substantive provisions" of ERISA. *Id.*[5]

The decision in *Nieto* is also internally inconsistent. Although the court refused to recognize a claim under the Act against a non-fiduciary knowing participant, it did rule that a non-fiduciary can be liable in an action

[5] Hewitt argues that make-whole relief is a "damages" remedy not included in the term "equitable relief" in section 1132(a)(3). In *United States v. Mitchell*, 463 U.S. 206 (1983), however, this Court held that damages were an available remedy for breach of trust: "It is well established that a trustee is accountable in damages for breaches of trust. See Restatement (Second) of Trusts, secs. 205-212 (1959); G. Bogert & G. Bogert, Law of Trusts and Trustees, sec. 862 (2d ed. 1965); 3 A. Scott, Law of Trusts, sec. 205 (3d ed. 1965)." *Id.* at 226. The Court implied a damages remedy for breach of trust because "prospective equitable remedies are totally inadequate [to protect beneficiaries]." *Id.* at 227. See also, e.g., G. Bogert & G. Bogert, Law of Trusts and Trustees, sec. 862 (2d ed. 1982) at 27: "For breach of trust the trustee may be **directed by the chancellor** to make a payment of damages to the beneficiary. . . . Acts of "negligence or misconduct in the making or retaining of investments may give rise to a right in favor of the beneficiaries to recover money damages from the trustee." *Id.* at 30-31. (Emphasis added.)

brought pursuant to section 1132(a)(3) when the non-fiduciary acts as a "party in interest" (29 U.S.C. § 1002(14)(b)) and engages in a prohibited transaction (29 U.S.C. § 1106(a)).[6] The court acknowledged that the broad equitable relief provided in section 1132(a)(3) (and therefore section 1132(a)(5)) "is not limited to fiduciaries." *Id.* at 874. The court held that equitable relief can be obtained against parties in interest that benefit from engaging in prohibited transactions, despite the fact that ERISA does *not* expressly bar parties in interest from engaging in prohibited transactions or explicitly provide relief from them for such actions. The court reasoned that "[c]ourts may find it difficult or impossible to undo such illegal transactions unless they have jurisdiction over all parties who allegedly participated in them." *Id.*

Finally, the language of sections 1132(a)(3) and (5) provides no basis to read those provisions so as to permit lawsuits against non-fiduciaries who engage in prohibited transactions, but not against those who knowingly participate in fiduciary breaches. The Ninth Circuit's interpretation provides inadequate protection for employee benefit plans because not all non-fiduciary participants in fiduciary breaches are parties in interest and not all fiduciary breaches are prohibited transactions.

[6] ERISA Section 406, 29 U.S.C. § 1106, which prohibits a "fiduciary" from causing an ERISA plan to engage in a prohibited transaction with a "party in interest" does not, by its express terms, provide a remedy against the non-fiduciary party in interest. Nor does section 1132. Nevertheless, the Ninth Circuit inferred the liability of the party in interest under section 1132(a)(3).

III. THE NINTH CIRCUIT'S NARROW CONSTRUCTION OF ERISA AND REFUSAL TO INCORPORATE NON-FIDUCIARY LIABILITY FOR KNOWINGLY PARTICIPATING IN A BREACH OF FIDUCIARY DUTY THREATENS EFFECTIVE PROTECTION OF EMPLOYEE BENEFIT PLANS.

The Ninth Circuit's interpretation of ERISA provides beneficiaries and participants with substantially less protection than they had before ERISA was enacted. Prior to ERISA, under the law of trusts, courts imposed liability on third persons who knowingly assisted or participated in a breach of fiduciary duty. ERISA was a reform statute. It would be paradoxical if it were interpreted to provide less protection to pension plan participants and beneficiaries than they had before ERISA.

Liability of non-fiduciaries who knowingly participate in breaches of fiduciary duty is essential to the complete protection of participants and beneficiaries. Trustees often cannot carry out violations of ERISA without the active cooperation of third parties. Third party liability is also important to provide complete relief. The trustees may be judgment proof or otherwise unable to provide complete relief restoring fully all losses suffered by a plan. Congress clearly did not intend to eliminate this protection, which was deemed essential even before the passage of ERISA.

A. Under the Law of Trusts, Third Persons Who Knowingly Assist in Breaches of Fiduciary Duty Are Liable to the Trust Beneficiaries.

The common law of trusts imposes liability on third persons who knowingly participate in a breach of trust. A trust beneficiary has a reasonable expectation that third persons have a duty not to knowingly participate in a breach of trust. *See* G. Bogert & G. Bogert, *The Law of Trusts & Trustees*, section 326 (1959) (third person who knowingly participates in breach of trust is liable to beneficiary for any loss thereby caused). *See also* Scott, *Participation in a Breach of Trust*, 34 Harv. L. Rev. 454, 481 (1921) (trust law places liability on third person for knowingly participating with fiduciary in breach of trust).

At common law, "[c]ourts will always impose liability for knowing participation in any fiduciary breach of duty." Comment, *Nieto v. Ecker, Incorporation of Nonfiduciary Liability Under ERISA*, 73 Minn. L. Rev. 1303, 1311 (1989). Prior to ERISA, both state and federal courts imposed such liability in order to fully protect trust beneficiaries. *See, e.g., Jackson v. Smith*, 254 U.S. 586, 589 (1920) (holding non-fiduciaries who joined fiduciary in sale of trust property to trustee jointly and severally liable for profits obtained); *Lawrence Warehouse Co. v. Twohig*, 224 F.2d 493, 498 (9th Cir. 1955) (stating that third person who colludes with fiduciary in committing breach of duty is under duty of restitution to beneficiary); *Whitford v. Reddeman*, 196 Wis. 10, 22, 23, 219 N.W. 361, 365-66 (1928) (recognizing court's power to enforce trust, complete trustee accounting, and hold liable those who assist trustee in violation of trust); *Massie v. Barth*, 634 S.W.2d 208, 211 (Mo. Ct. App. 1982) (holding that third party who has notice that trustee is committing breach of trust and participates with trustee is liable to beneficiary for any loss caused by breach of trust).

The imposition of non-fiduciary liability was thought important for the full protection of the beneficiary. Non-

fiduciary third persons often participate in the trustee's breach of fiduciary duty.[7] Perhaps even more critical, fiduciaries depend on active cooperation from non-fiduciary third parties to enable them to carry out breaches of fiduciary duty. *See, e.g.*, Stone, *The Public Influence of the Bar*, 48 Harv. L. Rev. 1, 19 (1934) (arguing violations of fiduciary duty do not usually occur without active assistance of others). It was against this background of common law liability that ERISA was enacted in order to provide more complete protection to the participants and beneficiaries of employee benefit plans.

[7] *See Jackson v. Smith*, 254 U.S. 586, 589 (1921) (third party participated in trustee's sale of trust property); *Carter Oil Co. v. Crude Oil Co.*, 201 F.2d 547, 551 (10th Cir. 1953) (non-fiduciary who knew co-tenant intended to misappropriate payments that should be shared by another co-tenant may be liable for participating in breach of trust); *Marshall v. Lovell*, 19 F.2d 751, 753 (8th Cir. 1927), *cert denied*, 276 U.S. 616 (1928) (trustee bribed by non-fiduciary); *Blankenship v. Boyle*, 329 F. Supp. 1089, 1096 (D.D.C. 1971) (union participated in conspiracy with employee welfare fund trustees and bank president and knowingly allowed plan funds to be held in interest-free accounts); *Malmud v. Blackman*, 278 N.Y. 658, 16 N.E.2d 391 (1938) (*per curium*) (non-fiduciary borrower who accepted usurious loan from trustee held liable for all loss caused to estate); *Zagrans v. Cohn*, 404 Pa. 315, 319, 172 A.2d 291, 293 (1961) (non-fiduciary sellers who induced trustee to make illegal investment held jointly and severally liable for losses of trust property, when they knew or ought to have known of breach of trust although purchase was in name of trustee without trust label); *Whitford v. Reddeman*, 196 Wis. 10, 24, 25, 219 N.W. 361, 366 (1928) (third party aided trustee in deceiving beneficiaries of investment trust regarding financial stability of trust).

B. Third Party Liability Under ERISA for Participation in Breaches of Fiduciary Duty is Necessary for the Effective Protection of Participants and Beneficiaries

In interpreting and applying ERISA, most federal courts have recognized that rejection of non-fiduciary liability is inconsistent with the remedial purposes of the Act. In conformity with pre-ERISA trust iaw, the vast majority of federal courts have held that ERISA includes a non-fiduciary liability standard for knowing participation in a fiduciary's breach of trust.[8]

This incorporation of non-fiduciary liability is consistent with the entire history and purpose of ERISA. It was the need to better protect plan participants that spurred the passage of ERISA and inspired the Congressional mandate for the courts to develop a "federal common

[8] *See Brock v. Hendershott*, 840 F.2d 339, 342 (6th Cir. 1988); *Lowen v. Tower Asset Management Inc.*, 829 F.2d 1209, 1220-1221 (2d Cir. 1987); *Fink v. National Sav. & Trust Co.*, 772 F.2d 951, 958 (D.C. Cir. 1985); *Thornton v. Evans*, 692 F.2d 1064, 1078 (7th Cir. 1982); *Dole v. Compton*, 753 F. Supp. 563, 565-569 (E.D. Pa. 1990); *Pension Ben. Guar. Corp. v. Ross*, 733 F. Supp. 1005, 1008 (M.D. N.C. 1990); *Pension Fund-Mid Jersey Trucking Industry-Local 701 v. Omni Funding Group*, 731 F. Supp. 161, 176-179 (D.N.J. 1990); *Brock v. Gerace*, 635 F. Supp. 563, 566 (D.N.J. 1986); *Foltz v. U.S. News & World Report, Inc.*, 627 F. Supp. 1143, 1167-1168 (D.D.C. 1986); *Donovan v. Schmoutey*, 592 F. Supp. 1361, 1395-1396 (D. Nev. 1984); *Donovan v. Bryans*, 566 F. Supp. 1258, 1266-1267 (E.D. Pa. 1983); *Donovan v. Daugherty*, 550 F. Supp. 390, 410-411 (S.D. Ala. 1982); *Freund v. Marshall & Ilsley Bank*, 485 F.Supp. 629, 641-642 (W.D. Wis. 1979). *See also Whitfield v. Lindemann*, 853 F.2d 1298 (5th Cir. 1988), *cert denied sub nom. Klepak v. Dole*, 490 U.S. 1089 (1989) (court assumes but does not expressly determine the existence of such liability).

law" in the enforcement of ERISA. Congress envisioned that a "body of [f]ederal substantive law [would] be developed by the courts to deal with issues involving rights and obligations under private welfare pension plans," 120 Cong. Rec. 29,942 (1974) (statement of Senator Javits), and that the federal courts would adapt trust law to the particular purposes of employee benefit plans. *See* S. Rep. No. 127, 93d Cong., 2d Sess. 29, reprinted in 1974 U.S. Code Cong. & Admin. News 4838, 4865. While the statute was detailed, the courts were needed to give it flesh and blood in actual operation. "But Congress realized that the bare terms, however detailed, of these statutory provisions would not be sufficient to establish a comprehensive regulatory scheme. It accordingly empowered the courts to develop, in the light of reason and experience, a body of federal common law governing employee benefit plans." *Menhorn v. Firestone Tire and Rubber Co.*, 738 F.2d 1496, 1499 (9th Cir. 1984). *See Firestone Tire and Rubber Co. v. Bruch*, 489 U.S. 101, 109 (1989) ("We have held that courts are to develop a 'federal common law of rights and obligations under ERISA-regulated pension plans' ").

The ability to hold third parties responsible for active participation in breaches of duty by fiduciaries is critical to the remedial purposes of ERISA. As mentioned above, non-fiduciaries participate in many fiduciary breaches. Furthermore, in many cases, fiduciaries simply will not be able to carry out such breaches without the active cooperation of third persons. The present case provides a vivid illustration of this fact. Petitioners allege that Hewitt, contrary to its professional responsibilities as the

Plan's actuary, knowingly aided and abetted the fiduciaries in allowing the severe underfunding of the Kaiser Steel Retirement Plan. Hewitt acted so as not to jeopardize its lucrative professional relationship with Kaiser on other matters. As a consequence of Hewitt's acts and omissions, the PBGC was forced to terminate the Plan pursuant to ERISA's distress termination procedures. The petitioners and all of the other participants and beneficiaries of the Plan suffered substantial losses in their retirement income.

Courts have recognized, both before and after the enactment of ERISA, that non-fiduciary liability is necessary to provide complete relief to participants and beneficiaries of employee benefits. *See Brock v. Gerace, supra*, at 569: "In the present case, the Local 564 dental plan's participants and beneficiaries *would be denied full relief* if the secretary were unable to recover from [knowingly participating] non-fiduciaries. . . . " (emphasis added); *see also Freund v. Marshall & Ilsley Bank*, 485 F. Supp. 629, 641-642 (W.D. Wis. 1979) (plan fiduciaries permitted the plan to loan all of its assets back to the sponsoring companies in exchange for unsecured promissory notes); *Lowen v. Tower Asset Management Corp, Inc., supra*, 829 F.2d at 1220-1221 (recognizing necessity of non-fiduciary liability under ERISA to pierce corporate form and prevent channeling of profits from fiduciary breaches to non-fiduciary entities to insulate them from liability under ERISA).

Given that non-fiduciary liability is necessary to fulfill the purpose of ERISA to protect plan participants and beneficiaries, surely the broad remedial provisions of ERISA encompass this basic remedy. The remedy is not

incidental; it goes to the core of ERISA's protection. Congress did not intend to exclude it from the remedies a federal court may give in enforcing ERISA. "[N]o sound reason appears why ERISA should be emasculated by a construction which precludes civil actions against non-fiduciaries." *Brock v. Gerace, supra,* 635 F. Supp. at 569.

CONCLUSION

For the reasons set forth above, petitioners urge that this Court grant the writ.

Respectfully submitted,

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